

IN THE
Supreme Court of the United States

MICHAEL T. KENNEDY, PETITIONER

v.

SKADDEN ARPS SLATE MEAGHER & FLOM LLP;
SKADDEN ARPS SK PRIVATE INVESTMENT FUND
1998 c/o SKADDEN ARPS; RICHARD T. PRINS;
GREGORY M. GALARDI; TENNENBAUM CAPITAL
PARTNERS, LLC; MICHAEL E. TENNENBAUM;
SUSAN S. TENNENBAUM; DAVID HOLLANDER;
ALVAREZ & MARSEL LLC; TENNENBAUM SVEF
LLC; TENNENBAUM SVOF LLC; MARK
HOLDSWORTH; HOWARD LEFKOWITZ; BABSON &
CO.; RICHARD E. SPENCER; JOSE E. FELICIANO;
STANLEY SPRINGEL; SK PRIVATE INVESTMENT
FUND 1998 LLC

*PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT*

REPLY BRIEF

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INTRODUCTION

Section 327(a) of the United States Bankruptcy Code authorizes the bankruptcy trustee to retain professional persons, such as attorneys, to represent the debtor, provided they “do not hold or represent an interest adverse to the estate” and they are “disinterested” within the meaning of 11 U.S.C. § 101(14), which defines a “disinterested person” as someone who “is not a creditor, an equity security holder, or an insider.” *See* 11 U.S.C. §§ 327(a), and 101(14)(A). Writing for the Third Circuit about 11 U.S.C. § 327(a), Justice Alito held in *United States Trustee v. Price Waterhouse*, 19 F.3d 138 (3d Cir. 1994), that “[a]s the Supreme Court and our court have repeated many times in recent years, when statutory language is clear and unambiguous it ordinarily must be followed.”

Here, the relevant statutory provisions of 11 U.S.C. § 327(a) are just as clear and unambiguous as they were 25 years ago in *Price Waterhouse*, but when it came to ownership by twenty-three attorneys of debtor’s counsel in the existing creditor who was negotiating to purchase, and ultimately did purchase, substantially all of the debtor’s assets, the statute was not followed. The reason it was not followed was that debtor’s counsel did not disclose it held an interest adverse to the estate until after expiration of all applicable statutes of limitation, and then, confronted with these admitted and undisputed facts, the courts below did nothing. This case therefore warrants the grant of *certiorari* in order to exercise this Court’s supervisory authority.

**I. SKADDEN'S OWNERSHIP WAS NOT
*DE MINIMIS***

Recognizing that an undisputed ownership interest in debtor's senior lender, credit bidder and ultimate purchaser in the sale transaction cannot be squared with the clear and unambiguous statutory language of 11 U.S.C. § 327(a), Respondents Skadden, Arps, Slate, Meagher & Flom, LLP ("Skadden"), as debtor counsel, and Tennenbaum, on behalf of the creditor, oppose *certiorari* by trying to convey the impression that "multiple courts" below found Skadden's ownership interest in Tennenbaum's affiliate to be "*de minimis*." In fact, the proposition that Skadden's ownership here was "*de minimis*" has never been tested by any court, while the failure to address the violation of Section 327(a) – and the claims resulting therefrom -- is an error of law that can only be addressed by *certiorari*.

The idea that Skadden's ownership in Special Value Expansion Fund ("SVEF") was "*de minimis*" was introduced by Skadden in its June 22, 2018 opposition to the instant petition for *certiorari*. See Skadden Opposition Brief ("Opp. Br.") at 9 (Skadden's March 2013 disclosure was "regarding *de minimis* interests certain Skadden partners and their spouses, in their individual and personal capacities, previously held in Tennenbaum funds, including \$19,500 in shares of Special Value Expansion Fund"); at 23 (petition rests on false allegations that "*de minimis* investments by Skadden partners and their spouses in certain Tennenbaum-affiliated fund were not adequately disclosed"). Even though it waited until after all applicable statutes of limitation had expired before disclosing its ownership, Skadden suggests there's

nothing to look at here because its partners held the interest – not the firm – and because the book value of their ownership interest was relatively small, although by what measure it does not say.

Skadden has always downplayed the significance of its March 2013 disclosure. While it waited until 2013 to admit ownership of SVEF dating back to 2004, it characterized SVEF as a “pre-petition lender.” However, it is undisputed that when Skadden sought approval in 2006 to become debtor’s counsel, SVEF was not only one of debtor’s senior secured lenders, SVEF credit bid its secured bonds to purchase substantially all of debtor’s assets, in a transaction negotiated by Skadden, as debtor’s counsel, thus placing Skadden on both sides of the transaction. It is also undisputed that the class of shares was issued only to Skadden partners (A1243), and ownership in that class gave them rights to control the lender’s board of directors. (A627-630).

Skadden nevertheless implies that “multiple courts” had rejected the suggestion that its ownership in SVEF was anything other than *de minimis*. See Opp. Br. at 10 n. 5 (Petitioner’s share ownership calculations are “not true and multiple courts previously have rejected Petitioner’s similar allegations”); at 2 (“all such alleged ‘new evidence’ previously was disclosed by Skadden and considered and ruled upon by the Bankruptcy Court and then the appellate courts in the last round of appeals”), at 18 (Petitioner’s contentions “were considered and rejected below on multiple occasions”), at 22-23 (Petitioner’s failure to meet its burden to show equitable tolling was found by “multiple courts”); at 27 (the argument that Skadden was not disinterested as required by 11 U.S.C.

§ 327(a) “has been rejected multiple times by multiple courts”).

However, there were no such findings. Nor did any court below define “*de minimis*” in this context or otherwise attempts to reconcile Skadden’s ownership of SVEF with “the plain language” of 11 U.S.C. § 327(a). *See Price Waterhouse*, 19 F.3d at 141.

Instead, Skadden clings to the district court’s February 9, 2017 decision dismissing Petitioner’s complaint, in which the court summarized Skadden’s March 2013 statement as “disclosing that, in 2004, 39 shares of a *Tennenbaum affiliate* were purchased by 23 Skadden partners and their spouses at \$500 per share, for an aggregate of \$19,500, and that *these were individual personal investments* as to which Skadden itself was not a party.” (emphasis added). *In re Radnor Holdings Corp.*, 564 B.R. 476, 481 (Del. 2017). The district court’s holding shows what went wrong: (1) it nowhere mentions that the Tennenbaum affiliate was SVEF; (2) it does not mention that SVEF was the debtor’s senior secured lender with whom Skadden, as debtor’s counsel, had been negotiating the sale of substantially all of debtor’s assets; and (3) it denied Petitioner’s request for discovery to obtain more information about the full extent of Skadden’s ownership of SVEF. 564 B.R. at 487.

The same thing happened when Petitioner’s complaint was dismissed by the bankruptcy court. Thus, in its April 22, 2016 decision, the Bankruptcy Court made no mention at all of the March 2013 disclosures. The court there simply accepted Skadden’s representations that the only applicable statutes of limitation that matter were based on state law, and held that Petitioner’s claims were both time-barred and barred by the court’s prior ruling granting Skadden’s

fee application, which had been affirmed on appeal. *See In re Radnor Holdings Corp.*, Case No. 06-10894 (KG); Adv. No. 12-31308, 2016 WL 164499 (Del. Bankr. April 22, 2016).

Neither of the two decisions of the Third Circuit – the one on Skadden’s fee application, *In re Radnor Holdings Corp.*, 629 Fed. Appx. 277 (3d Cir. 2015) and the one affirming the dismissal of Petitioner’s complaint, *In re Radnor Holdings Corp.*, 706 Fed. Appx. 94 (3d Cir. 2017) -- addressed Skadden’s ownership interests in SVEF and the mandatory requirements of 11 U.S.C. § 327(a). Thus, in ruling that the bankruptcy court did not abuse its discretion in granting Skadden’s final fee application, the Third Circuit said Petitioner had alleged that “Skadden failed to disclose in its application to the Bankruptcy Court certain investments in Tennenbaum and its affiliates” -- without identifying the specific “affiliate,” the crucial role it played in debtor’s bankruptcy, and Skadden’s having waited seven years, until after expiration of all applicable statutes of limitation, before disclosing it. 629 Fed. Appx. at 279.

And when the Third Circuit affirmed dismissal of Petitioner’s complaint and held there was no reason to allow equitable tolling, there was again no discussion of Skadden’s ownership interest in SVEF, much less that such interest was “*de minimis*.” Instead, the Court of Appeals said Petitioner’s argument was that “appellees concealed, until March 15, 2013, that certain Skadden attorneys had ownership interests *in a Tennenbaum-affiliated Fund*” (emphasis added) and, having thus characterized the interest in that manner, the Court of Appeals dismissed on the ground that Skadden had already disclosed in 2006 that “Skadden partners had

invested in the Tennenbaum-affiliated Funds.” 706 Fed. Appx. at 98-99.

In short, in finding that equitable tolling was not applicable here, the Third Circuit did not mention the undisputed fact that Skadden waited until after expiration of the applicable statutes of limitation to disclose that the specific “Tennenbaum-affiliated Fund” that Skadden’s partners held an ownership interest in was the debtor’s existing senior secured lender and the ultimate purchaser of substantially all of debtor’s assets. This was information Skadden obviously knew about in 2006, when these events were taking place, but which Skadden elected not to disclose.

Had those facts not been overlooked or otherwise left unexamined, the Court of Appeals would have had to address the elephant in the room – and the essence of Petitioner’s appeal -- which was that such disclosure would not only have warranted Skadden’s automatic disqualification under 11 U.S.C. § 327(a), but it would also have warranted the application of equitable tolling to allow Petitioner’s otherwise time-barred complaint against Skadden and Tennenbaum challenging the negotiation and sale of those assets – in which Skadden was on both sides of the transaction -- to go forward.

II. SKADDEN’S ARGUMENTS UNDERScore WHY CERTIORARI IS APPROPRIATE

Skadden’s arguments notwithstanding, this case is indeed an appropriate vehicle for granting *certiorari*. No court in the long history of this dispute has ever addressed the issue of whether Skadden’s ownership of SVEF, the senior lender and ultimate purchaser, was a

disqualifying violation under 11 U.S.C. § 327(a). Nor has any court ever addressed the issue of whether, instead of waiting seven years until all applicable statutes of limitation had run, Skadden should have disclosed its ownership of SVEF in 2006, when it sought approval over objection by the United States Trustee to become debtor's counsel and again, soon after, when it sought approval over objection by the unsecured creditors of the sale of substantially all of debtor's assets.

Skadden argues that the Petition exaggerates its undisputed ownership interest in SVEF. Opp. Br. at 10 n. 5. ("Petitioner mischaracterizes the record through the Petition by falsely stating that the \$19,500 in shares of SVEF previously held by certain Skadden partners or their spouses, in their individual and personal capacities, establishes that Skadden 'owned' SVEF"). However, Skadden's partner Galardi testified that the class of shares Tennenbaum had offered to Skadden partners was for tax reasons offered only to Skadden partners and no one else. (A1243). And there is no disputing that the rights of those holding the class of shares that Skadden's partners held gave them a priority interest and the right to control the SVEF board if dividends were not paid for two years. (A627-630).

Furthermore, to place Skadden's arguments about its ownership of SVEF in context, Skadden successfully blocked Petitioner from obtaining any discovery in aid of its complaint, including discovery of the full extent of Skadden's ownership interests in SVEF, thereby raising due process concerns. Thus, Skadden blocked Petitioner from learning which specific Skadden partners owned SVEF, whether those partners had been representing Tennenbaum and

were adverse to Radnor, why their ownership interest was not disclosed in 2006 when Skadden was required to make such disclosure, whether the class of shares at issue – the so-called “Z” class – was owned exclusively by Skadden’s partners and no one else, as Galardi had testified and, even though the stated consideration for these shares was stated to \$19,500, whether the price was discounted as partial compensation for legal work, and then, when Skadden’s partners redeemed their interests in SVEF (after SVEF had succeeded in purchasing substantially all of the debtor’s assets, for what Petitioner contends was less than fair value, in a transaction negotiated by Skadden itself), how much remuneration each of those Skadden partners actually received for their \$19,500 investment.

Had Skadden complied with its obligations of disclosure in 2006, when it was seeking court approval to be debtor’s counsel for Radnor, or when, a few months later, it was seeking court approval for the sale of substantially all of Radnor’s assets to SVEF, Skadden could have argued then that its ownership interests in SVEF were *de minimis*. However, in light of the objections to its appointment that had already been lodged by the United States Trustee, and the clear and unambiguous language of 11 U.S.C. § 327(a), Skadden’s appointment then would almost certainly not have been approved, which suggests that Skadden’s lack of candor in 2006 was intentional. Thus, by withholding information as to its partners’ ownership of SVEF, which Skadden obviously had a duty to disclose, Skadden became debtor’s counsel, successfully sold substantially all of Radnor’s assets to SVEF, succeeded in fending off challenges that the terms of the sale were unfair to Radnor’s stakeholders and its other creditors, and then, years later, with Radnor having been

liquidated, Skadden received millions of dollars in fees – all for work that, pursuant to 11 U.S.C. § 327(a), it should never have been allowed to do in the first place.

Skadden argues that there is no basis for granting *certiorari* on Petitioner’s First, Third and Fourth Questions Presented – which concern the Third Circuit’s determination that equitable tolling was not warranted -- on the ground that they are all predicated on “false (and case specific) factual assertions and allegations that were considered and rejected below.” These arguments are without merit.

When a professional owns a creditor with a claim against an estate, it cannot act as debtor’s counsel without running afoul of 11 U.S.C. § 327(a) which expressly bars trustees from retaining professionals which hold an interest “adverse to the estate.” Here, Skadden cannot dispute that its partners (and their spouses) owned SVEF, at least in part; nor can it dispute that SVEF was the debtor’s senior secured lender, and that, as debtor’s counsel, Skadden negotiated and ultimately solicited a bid from SVEF for the sale of substantially all of the debtor’s assets. Its only escape is not to concede that the courts below overlooked these undisputed facts, which they did, but rather to suggest that the courts below must have thought its ownership interest was “*de minimis*” because how else could they have ignored it? That *ex post facto* rationale is not a basis for denying *certiorari*. It is a reason why *certiorari* should be *granted*.

Skadden’s argues that the First, Third and Fourth Questions Presented do not merit *certiorari* on the ground that “[t]his Court is not the proper forum for second-guessing the *factual findings* of the Bankruptcy Court, which is, in essence, all that Petitioner requests.” Opp. Br. at 2. (emphasis added).

Skadden also suggests that those findings “rested, in part, on credibility determinations.” Opp. Br. at 19.

However, not only were there no “factual findings” that Skadden’s ownership of SVEF was “*de minimis*,” there could certainly have been no such finding based on a “credibility determination.” Skadden’s ownership interest was set forth in Skadden’s own written disclosure dated March 15, 2013, which was confirmed in testimony by Skadden partners over a two-day hearing in early May 2013 on Skadden’s fee application. The factual findings on the fee application did not mention the undisputed nature of the ownership interest that was disclosed in March 2013, and the court’s rulings blocked Petitioner from obtaining any discovery to demonstrate just how substantial and significant that ownership interest actually was.

Skadden nevertheless argues that “[t]he March 2013 Disclosure was not ‘overlooked’ by the Bankruptcy Court, but rather was squarely before, and ruled upon, by the Bankruptcy Court in the Final Fee Order, which is a final and non-appealable order.” Opp. Br. at 19. But Skadden can cite no finding that takes into account the *undisputed facts* that Skadden owned an interest in SVEF, SVEF was the debtor’s senior secured lender that was negotiating for and ultimately acquired substantially all of the debtor’s assets, in a transaction in which Skadden represented the debtor’s estate, thus placing it on both sides of the transaction – and, because none of this was known until after expiration of all applicable statutes of limitation, placing the doctrine of equitable tolling squarely at issue.

Skadden’s arguments with respect to the Second Question Presented are likewise without merit. Skadden first argues that the application of Section

327(a) was “not properly before” the Third Circuit because Petitioner’s claims had been dismissed as time-barred. Opp. Br. at 25. That, of course, begs the question. The issue is whether the federal statutory requirement of “disinterestedness” can be avoided if a law firm waits until after expiration of all applicable statutes of limitation to disclose disqualifying information it obviously knew about before any statutes of limitation began to run. That is an issue of law.

Skadden next argues that, as with the First, Third and Fourth Questions Presented, “the Petition is an “exceptionally poor vehicle” for reviewing the Second Question Presented because consideration of that question is barred by *res judicata*, collateral estoppel and waiver.” Op. Br. at 29. However, no such iron-clad bar exists. Thus, for example, there is no bar to courts re-considering otherwise final and non-appealable orders which were issued based on a “fraud on the court” see Fed. R. Civ. P. 60(d)(3), or to prevent a “grave miscarriage of justice.” See *U.S. v. Beggerty*, 524 U.S. 38, 47 (1998).

Finally, Skadden suggests that Petitioner’s arguments as to Skadden’s ownership of SVEF were so off the mark that Petitioner was “sanctioned” for having raised them in the first place. See Opp. Br. at 1 (“Petitioner was *recently sanctioned* by the Bankruptcy Court for “litigat[ing] beyond reason” and for his false allegations concerning Respondents”). The Bankruptcy Court order cited was issued more than three years ago, on March 18, 2015, in denying a motion by Petitioner to vacate a prior order of the bankruptcy court granting Skadden’s fee award. The court’s order merely directed Petitioner to make any further arguments to the appellate courts, which is exactly what he did. Op. App. 63a-64a.

CONCLUSION

For the foregoing reasons, and the reasons set forth in his Petition, Petitioner Michael T. Kennedy respectfully requests that *certiorari* be granted.

Respectfully submitted,

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